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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1949

No. 444

CALIFORNIA STATE AUTOMOBILE ASSOCIATION,
Petitioner,

vs.

JAMES G. SMYTH, Collector of Internal Revenue of the First Internal Revenue Collection District of California,
Respondent.

PETITION FOR WRIT OF CERTIORARI to the United States Court of Appeals for the Ninth Circuit and BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI to the United States Court of Appeals for the Ninth Circuit.

To the Honorable Fred M. Vinson, Chief Justice of the United States, and to the Honorable Associate Justices of the Supreme Court of the United States:

Your petitioner, California State Automobile Association, prays that a writ of certiorari issue to review the

final judgment of the United States Court of Appeals for the Ninth Circuit determining that petitioner was not, during the years 1943 and 1944, a club exempt from income taxation by Section 101(9) of the Internal Revenue Code.

OPINIONS BELOW.

The opinion of the Court of Appeals (R. 226) is reported at 175 Fed. (2d) 752. The opinion of the District Court (R. 67) is reported at 77 Fed. Supp. 131.

JURISDICTION.

The judgment of the Court of Appeals for the Ninth Circuit was entered on June 22, 1949. (R. 234.) That Court denied petitioner's Petition for Rehearing on August 8, 1949. (R. 235.) The jurisdiction of this Court is invoked under Title 28, United States Code, Section 1254(1).

QUESTION PRESENTED.

Was petitioner a club organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder (member), and thus entitled to exemption from income and excess profits taxes for the years 1943 and 1944, as well as for future years, under the provisions of Section 101(9) of the Internal Revenue Code.

STATUTES INVOLVED.

Internal Revenue Code, 52 Stat. 480, 481:

"Section 101. *Exemptions From Tax on Corporations.*

"The following organizations shall be exempt from taxation under this chapter:

* * * * * * *

"(9) Clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder."

STATEMENT.

Petitioner is a non-profit, non-stock corporation, organized in 1907 under the laws of the State of California. (R. 67.) From 1913, when the first income tax law was enacted under the 16th Amendment, until 1943, a period of 30 years, petitioner had been exempt from the payment of income and excess profits taxes. (R. 68.) That exemption was finally withdrawn by the Commissioner of Internal Revenue by letter dated July 25, 1945 (Exhibit 1, R. 15-18), in which petitioner was informed it would be "required to file income tax returns and pay any tax shown to be due thereon for each of your taxable years beginning on or after January 1, 1943." This action by the Commissioner was taken in spite of the fact that there had been no change in the law since 1916 except an immaterial change in terminology from "private stockholder or member" to "private shareholder", and no sub-

stantial change in the Regulations except to broaden the terms of exemption in favor of taxpayers. (R. 74.)

Petitioner then filed income and excess profits tax returns, under protest, with respondent for the years 1943 and 1944, and paid the taxes shown thereon, with interest to date of payment. (R. 81.) Thereupon petitioner filed with respondent claims for refund of the amounts so paid and, the Commissioner of Internal Revenue having taken no action either approving or rejecting any of said claims within 6 months from the dates said claims were filed, a suit for refund of the aforesaid amounts of taxes and interest paid was filed in the District Court of the United States for the Northern District of California, under the provisions of Section 3772(a)(2) of the Internal Revenue Code. (R. 2-63, 81-82.) Thereupon respondent filed an answer. (R. 63-67.) The trial was by the Court and judgment was rendered in favor of petitioner against respondent. (R. 79.) An appeal from said judgment was taken by respondent to the Court of Appeals for the Ninth Circuit (R. 91, 92), which reversed the judgment of the District Court. (R. 234.)

The District Court made findings of fact and conclusions of law. (R. 80-89.) It found that the purposes of petitioner have been practically unchanged since its organization, and at all times pertinent were substantially to promote and encourage highway construction, improvement, betterment, maintenance and marking for the guidance and warning of the users, to urge adoption of just and intelligent legislation on the use

of highways and the regulation of traffic thereon, to maintain offices for collecting and disseminating information and the furnishing of advice and assistance to the owners of automobiles, to protect the legitimate interests of its members in connection with its purposes, to affiliate and associate with similar organizations; that none of the foregoing or any other purposes of petitioner were designed or intended to make a profit; that petitioner has no power to distribute or set aside any portion of its net income to its members or to any other person except to carry out its purposes; that in furtherance of the purposes for which it was originally organized as an automobile club, petitioner has provided during the years 1943 and 1944 as well as prior and subsequent to said years, (1) a Touring Bureau which provides the members with complete touring data and assists them in planning motor trips; (2) an Emergency Road Service Department, which makes arrangements for the rendering of emergency road service to members who encounter automobile trouble on the highways, which service is restricted to passenger cars; (3) a Road Sign Department, which operates in conjunction with state and local authorities a service consisting of the erection and maintenance of direction and warning signs and historical markers; (4) a Public Safety Department, which carries on an active aggressive campaign to reduce traffic accidents, eliminate traffic hazards and generally improve traffic conditions; (5) an Adjustment and Traffic Department, which advises and assists the members with respect to traffic viola-

tions and accidents; (6) a License Department, which assists members in the annual renewal of automobile registration with the State Department of Motor Vehicles and obtaining automobile license plates, as well as Federal auto tax stamps; and (7) a Magazine Department which publishes and distributes free to the members a magazine, keeping them informed of motoring conditions and improvements, and specializing in travel information with respect to trips to points of interest where members will find pleasure and recreation, and which has contained no paid advertising material since January 1, 1942; there is no sale or public distribution of said magazine; that the sum total of the activities of the petitioner is designed to alleviate the occasional hardships and inconveniences which are connected with the ownership and operation of pleasure automobiles, and the services rendered by petitioner are for the pleasure and recreation of its members; that, in addition to the normal activities and services of the petitioner during the two years here in question, petitioner engaged in many activities incidental to the war effort and performed many services for the general public, such as road signing as an official agency of the Federal Government in blackout and dimout areas, services in connection with gas rationing, information and advice furnished members of the armed forces, training of drivers for the Red Cross and other volunteer war services, and in arrangements of reservations and accommodations for its members; that none of the normal activities or the wartime activities of the

petitioner were conducted for the purpose of earning a profit or accumulating a surplus, nor was any profit derived from any of these activities; that the petitioner is and was at all times pertinent a club within the meaning of Section 101(9) of the Internal Revenue Code; that petitioner was organized and operated exclusively for pleasure, recreation and other nonprofitable purposes during the years 1943 and 1944, and that no part of its net earnings during said years inured to the benefit of any of its members. (R. 82-89.)

The principal question before the Court of Appeals was whether this petitioner was, during the years 1943 and 1944, a club, organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inured to the benefit of any private shareholder (member). Petitioner timely filed a petition for rehearing in the Court of Appeals, but said petition was denied on August 8, 1949. (R. 235.)

REASONS FOR GRANTING THE WRIT.

1. The Court of Appeals for the Ninth Circuit has decided an important question of Federal law which has never been, but should be, settled by this Court.

The same question of Federal law is presently involved in the cases of a very large number of automobile clubs throughout the United States.

A decision by this Court in this case is required to determine the future, as well as the past, status of petitioner under the aforesaid Section 101(9). Such a decision would presumably likewise set up certain standards by which the tax exemption under the said Section of a large number of other automobile clubs throughout the nation could be determined, thus avoiding a considerable volume of litigation. An important question remains to be determined, one which can be resolved only by this Court, viz., is the nationwide and traditional classification of automobile clubs now to be abrogated?

2. Indicative of the importance of the Federal question involved was the statement of Government Counsel, at the outset of his argument in the Court of Appeals, that this is the Government's test case in obtaining an interpretation of Section 101(9) of the Internal Revenue Code.

3. The Court of Appeals has decided several Federal questions in a way probably in conflict with applicable decisions of this Court.

(a) The Court of Appeals has failed to apply decisions of this Court that where there have been later re-enactments of a section of a tax statute, Congress must be taken to have approved the administrative construction and thereby to have given it the force of law.

Helvering v. Bliss, 293 U.S. 144, 79 L.Ed. 246;
Helvering v. R. J. Reynolds Tobacco Co., 306 U.S. 110, 59 S.Ct. 423;

Helvering v. Griffiths, 318 U.S. 371, 63 S.Ct. 636.

(b) The Court of Appeals has failed to give effect to Rule 52(a) of the Rules of Civil Procedure for the District Courts of the United States, providing in part:

> "Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses."

Discussing the principle of the aforesaid rule, long recognized and applied by courts of equity, Mr. Justice Holmes in *Adamson v. Gilliland,* 242 U.S. 350, 353, 37 S.Ct. 169, 170, 61 L.Ed. 356, citing *Davis v. Schwartz,* 155 U.S. 631, 636, 15 S.Ct. 237, 39 L.Ed. 289, said

> "* * * the case is preeminently one for the application of the practical rule that so far as the finding of the master or judge who saw the witnesses depends upon conflicting testimony or upon the credibility of witnesses, or so far as there is testimony consistent with the finding, it must be treated as unassailable."

CONCLUSION.

Wherefore, it is respectfully submitted that this petition for a writ of certiorari should be granted to review the judgment of the Court of Appeals for the Ninth Circuit.

Dated, San Francisco, California,
October 31, 1949.

CALIFORNIA STATE AUTOMOBILE ASSOCIATION (a corporation),
Petitioner.

By ARTHUR H. DEIBERT,
Counsel for Petitioner.

GEORGE E. SANDFORD,
DEMPSEY, THAYER, DEIBERT & KUMLER,
Of Counsel.

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No.

CALIFORNIA STATE AUTOMOBILE ASSOCIATION,
Petitioner,

vs.

JAMES G. SMYTH, Collector of Internal Revenue of the First Internal Revenue Collection District of California,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

May It Please The Court:

OPINIONS OF COURTS BELOW.

The opinion of the Court of Appeals (R. 226) is reported at 175 Fed. (2d) 752. The opinion of the District Court (R. 67) is reported at 77 Fed. Supp. 131.

JURISDICTION.

The grounds upon which the jurisdiction of this Court is invoked are stated in the petition at page 2.

STATEMENT OF THE CASE.

The facts appear in the petition at pages 2 to 6 and in the interest of brevity are not repeated herein.

However, a brief reference to the nature of the controversy is pertinent in presenting the major federal issues raised in the case at bar.

Petitioner is a corporation claiming income tax exemption as a club organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder (member). Exemption is claimed under Section 101(9) of the Internal Revenue Code, 52 Stat. 480, 481.

For a period of thirty years, from 1913 to 1943, petitioner uninterruptedly had been accorded income tax exemption under practically identical provisions of the successive revenue laws, until such exemption was finally withdrawn by the Commissioner of Internal Revenue by letter dated July 25, 1945 (Exhibit 1, R. 15-18), requiring the filing of tax returns and the payment of taxes for taxable years beginning January 1, 1943.

Petitioner prevailed in the Federal District Court but that decision was reversed by the Court of Appeals for the Ninth Circuit.

SPECIFICATION OF ERRORS.

The Court of Appeals erred:

1. In failing to give any effect to decisions of this Court that where there have been later re-enactments of a section of a tax statute, Congress must be taken to have approved the administrative construction and thereby to have given it the force of law.

2. In failing to give any effect to Rule 52(a) of the Rules of Civil Procedure for the District Courts of the United States providing, in part, that findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial Court to judge the credibility of the witnesses.

SUMMARY OF ARGUMENT.

1. This case involves the determination of an important question of Federal law which should be settled by this Court.

2. The administrative construction of a provision of a tax statute acquires the force of law by subsequent re-enactments of such provision by Congress.

3. Under Rule 52(a) of the Rules of Civil Procedure for the District Courts of the United States, findings of the trial Court, so far as there is testimony consistent with the findings, are unassailable.

ARGUMENT.

1. THE CASE INVOLVES THE DETERMINATION OF AN IMPORTANT QUESTION OF FEDERAL LAW WHICH SHOULD BE SETTLED BY THIS COURT.

The vital importance to the more than three hundred automobile clubs throughout the United States, including petitioner, of a decision by this Court in this case is emphasized by the statement of Government counsel at the trial of the case in the District Court when he stated, "In connection with the failure of the Commissioner to act promptly after 1941, I take it, is explained by the fact that *this action was a national action taken as to all similar clubs in 1943* and had not been taken as to any of them prior to that time. There is no difference between 1941 and 1943, as far as this club is concerned, or any other club in the United States. That followed G.C.M. 23688 [1943 Cumulative Bulletin 283] which was issued in 1943. In other words, *it was a change at that time of the Department in reference to all clubs*". (Italics supplied.) (R. 106-107.)

The foregoing statement concerning the failure of the Commissioner to act promptly after 1941 relates to the fact that petitioner's general manager, in October, 1941, furnished the Government an affidavit (Exhibit 1-D, R. 112) which contained a statement regarding the activities of petitioner. This statement was requested by respondent on September 10, 1941 (Exhibit 1-C, R. 112), while the final ruling letter of the Commissioner denying petitioner exemption under Section 101(9) of the Internal Revenue Code was not issued until July 27, 1945. (Exhibit 1, R. 15-18.)

The question at issue has never been passed upon by this Court, and in view of the potentially large volume of litigation which otherwise may ensue, it is believed to be not only in the interest of this petitioner but of a very large number of additional automobile clubs throughout the United States to have this question decided by this Court in the present case. In rendering such a decision, it is believed this Court would necessarily set up certain standards which would enable a large number of other automobile clubs throughout the nation to ascertain their own tax status under Section ~~102~~ 101(9), supra, thus avoiding a considerable volume of litigation. At the present time a vital question remains to be authoritatively determined, one which can be resolved only by this Court, viz., is the nationwide and traditional classification of automobile clubs now to be abrogated? In fact, Government counsel in the Court of Appeals prefaced his argument by the statement that this is the Government's test case for the purpose of obtaining an interpretation of Section 101(9) of the Internal Revenue Code.

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2. THE ADMINISTRATIVE CONSTRUCTION OF A PROVISION OF A TAX STATUTE ACQUIRES THE FORCE OF LAW BY SUBSEQUENT REENACTMENTS OF SUCH PROVISION BY CONGRESS.

There has been no change in the tax statute here involved, Section 101(9) of the Internal Revenue Code, since 1916 with the exception of an immaterial change in terminology from "private stockholder or

member", to "private shareholder", the provision in question now reading as follows:

> "Section 101. *Exemptions from Tax on Corporations.*
>
> "The following organizations shall be exempt from taxation under this chapter:
>
> * * * * * * *
>
> "(9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder."

Likewise, there has been no substantial change in the regulations interpreting the foregoing provision from Regulations 33, Article 72, under the Revenue Act of 1916, to the present time, except to expand and broaden the terms of exemption as they appear in present Treasury Regulations 111, Section 29.101(9), in which the following sentence was added to the former regulations: "Generally, an incidental sale of property will not deprive the club of the exemption". (R. 74.)

For a period of thirty years, from 1913 to 1943, the Commissioner of Internal Revenue had exempted petitioner from the payment of any income tax under an administrative construction repeated again and again with no material change in a number of successive regulations issued under various revenue Acts, and finally under the codification of such Acts in the Internal Revenue Code. A number of decisions of this Court have established the rule that such admin-

istrative construction of a provision of a tax statute acquires the force of law by virtue of subsequent re-enactments by Congress of such provision.

This Court in *Helvering v. Bliss,* 293 U. S. 144, 79 L. Ed. 246, stated in connection with the right to a deduction on account of charitable contributions:

> "If the meaning of the Act were doubtful, we should still reach the same conclusion. The exemption of income devoted to charity and the reduction of the rate of tax on capital gains were liberalizations of the law in the taxpayer's favor, were begotten from motives of public policy, and *are not to be narrowly construed.* * * * Moreover, from 1923 to 1932 the Commissioner uniformly ruled that the deduction for charitable contributions was to be taken from net income before computation of the tax and hence in whole from ordinary net income. *The reenactment in later Acts of the sections permitting the deduction indicates congressional approval of this administrative interpretation.*" (Italics supplied.)

This Court again spoke on this question in *Helvering v. R. J. Reynolds Tobacco Co.,* 306 U.S. 110, 59 S.Ct. 423. In that case the Commissioner's regulations, in effect in 1929, provided that:

> "A corporation realizes no gain or loss from the purchase or sale of its own stock"

and they had so provided since 1920. This Court there said:

> "The administrative construction embodied in the regulation has, since at least 1920, been uniform

with respect to each of the revenue acts from that of 1913 to that of 1932, as evidenced by Treasury rulings and regulations, and decisions of the Board of Tax Appeals. In the meantime, successive revenue Acts have reenacted, without alteration, the definition of gross income as it stood in the Acts of 1913, 1916, and 1918. Under the established rule Congress must be taken to have approved the administrative construction and thereby to have given it the force of law."

In *Helvering v. Griffiths,* 318 U.S. 371, 396, 63 S.Ct. 636, this Court cited its decision in *Helvering v. Winmill,* 305 U.S. 79, 83, 83 L. Ed. 52, 55, 59 S.Ct. 45, as follows:

"Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received Congressional approval and have the effect of law".

In *Bryant v. Commissioner,* 111 Fed. (2d) 9, the Court of Appeals for the Ninth Circuit, itself said, in a case where an administrative practice by the Bureau of Internal Revenue had continued for more than twenty-two years, although a contrary opinion was later expressed in a memorandum of the General Counsel of that Bureau:

"The established administrative practice of so many years, during which time the exemption was several times reenacted, carries weight as a construction of the statute which is not offset, at least as to the tax year in question, by the later

expression of opinion in G.C.M. 16861, XV-2 Cum. Bull. 179 (1936)." (Italics supplied.)

In *Citizens National Trust & Savings Bank of Los Angeles v. United States,* 135 Fed. (2d) 527 (CCA-9), the bank contended that R. S. 3186 gave the United States a lien only upon property possessed by the taxpayer at the time of the distraint and that the lien did not attach to after-acquired property. The Court of Appeals for the Ninth Circuit held that the statute, by its terms, applied to after-acquired property but went on to say that if the statute was so general in its terms that an administrative interpretation was appropriate, the statute had been interpreted to apply to after-acquired property. Since such interpretation, the section had been amended with no addition of a definite provision as to after-acquired property and presumably with Congressional knowledge of the departmental interpretation. The Court said: "Therefore, such interpretation must be taken as approved by Congress."

The Court of Appeals in the case at bar has failed to give effect to the established rule above discussed.

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3. UNDER RULE 52(a) OF THE RULES OF CIVIL PROCEDURE FOR THE DISTRICT COURTS OF THE UNITED STATES, FINDINGS OF THE TRIAL COURT, SO FAR AS THERE IS TESTIMONY CONSISTENT WITH THE FINDINGS, ARE UNASSAILABLE.

There was a considerable volume of testimony presented to the District Court in this case consistent

with the findings of that Court that petitioner was a club (R. 112, 113, 143, 144, 153-155, and 176-182), organized and operated exclusively for pleasure, recreation, and other non-profitable purposes (R. 119-125, 129-133, 146-151, 157-166, 168-171, 182-184, and 189-212), no part of the net earnings of which inures to the benefit of any private shareholder. (R. 173, 174, 184, 186, 187, and 189.)

Consequently, the Court of Appeals erred in failing to adopt and follow the findings of the District Court under the principle enunciated in the foregoing Rule (52(a)). In holding contrary to some of such findings the Court of Appeals has completely ignored the authority of said Rule and, in addition, has given no effect to the phrase in said Section "and other non-profitable purposes", following the words "pleasure, recreation".

In *Wittmayer v. United States,* 118 Fed. (2d) 808, 811, the Court of Appeals for the Ninth Circuit said, in interpreting Rule 52(a), supra, and relying upon several decisions of this Court:

> "The provisions of the new procedural rules that the findings of fact of the trial judge are to be accepted on appeal unless clearly wrong (Rule 52(a), 28 U.S.C.A. following Section 723c), is but the formulation of a rule long recognized and applied by courts of equity. *Guilford Const. Co. v. Biggs,* 4 Cir., 102 F. (2d) 46, 47.
>
> "As was said by Mr. Justice Holmes in *Adamson v. Gilliland,* 242 U.S. 350, 353, 37 S.Ct. 169, 170, 61 L. Ed. 356 (citing *Davis Schwartz,* 155 U.S.

631, 636, 15 S. Ct. 237, 39 L. Ed. 289), the case is preeminently one for the application of the practical rule, that so far as the findings of the trial judge who saw the witnesses 'depends upon conflicting testimony or upon the credibility of witnesses, or *so far as there is any testimony consistent with the finding, it must be treated as unassailable.*'" (Italics supplied.)

See also *United States v. Aluminum Co. of America*, 148 F. (2d) 416, 433 (C.C.A. 2nd).

CONCLUSION.

Wherefore, it is respectfully submitted that this petition for a writ of certiorari should be granted and that this Honorable Court should review the decision of the United States Court of Appeals for the Ninth Circuit and finally reverse it.

Dated, San Francisco, California,
October 31, 1949.

ARTHUR H. DEIBERT,
Counsel for Petitioner.

GEORGE E. SANDFORD,
DEMPSEY, THAYER, DEIBERT & KUMLER,
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